M e m o r a n d u m

295.1930

To: Mr. J. J. Kontilis
Oakland – Compliance

Date: January 12, 1990

From: David H. Levine
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Subject: --- --- ---

This is in response to your memorandum dated December 12, 1989 regarding the application of tax to [A]'s activities of providing art to churches. You have included a letter from [A] as well as a letter from District Principal Auditor Jim Speed dated August 16, 1989 which summarizes his understanding of the relevant activities by [A]. The activities at issue are the temporary installation of art in churches and the supervision of the installation of art created by students.

Furnishing of Art by [A].

The art furnished by [A] apparently takes a great deal of thought and planning and involves a considerable effort to actually place in the church but apparently often involves the transfer of tangible personal property that may be of minimal value when acquired by [A] (e.g., paper, fabric, and string).

This is a lease since [A] retains ownership of the property and retakes possession of the tangible personal property at the end of the lease. Although much of the value of the transferred art is added through the efforts of [A], this is nevertheless the lease of tangible personal property just as would be a temporary transfer of a painting (the value of the bare canvas and paint may very well be minimal compared to the value of the completed painting). Since [A] will be leasing the art in a form not substantially the same as acquired, her lease is subject to use tax measured by rentals payable regardless of whether she paid sales tax reimbursement when purchasing the property. Of course, if she makes no other use of that property except these rentals (such use would include the temporary transfer of possession for no charge or an outright gift), she may purchase the property incorporated into the art ex tax for resale or take a tax-paid purchases resold deduction when appropriate.

The difficult question here is the amount of the taxable rentals payable for [A]'s leases. There are two aspects to this question: what amounts are required to be paid to [A] for the leases; and whether any of those amounts are excludable from tax.

Some of the churches agree to a specific dollar amount for [A]'s artwork. This agreed to amount is the measure of the taxable rentals payable. The other circumstances [A] describes in her letter to Mr. Speed as: "I do it as a gift…. The churches in return contribute to my life with the best that they can do, so that their money can enable my time to be continuously spent doing this work. They are reassuming the old role of patron of the artist in this act. It is an exchange of gifts, and there simply are no fees. I have no idea what I will be paid for any of this work." We do not agree that this is simply an exchange of gifts. From her description, it appears that she has agreed to supply the art in exchange for the church paying her something. That the amount is not certain does not mean that tax does not apply. Tax would apply in the same manner as royalties, that is, tax is due for the reporting period in which the amount becomes certain (except for a lease, if the amount becomes certain before it becomes payable, it is taxable when payable). This analysis would apply to transactions in which the church as agreed to pay [A] something, in an amount to be determined by the church or in an amount to be determined based upon some other agreed upon factors.

Please note, however, that this discussion is merely for your guidance. Our conclusion depends on the specific facts of each lease in question. If there were no agreement that the church would pay [A] something, even though uncertain, then we might agree that she was making a gift. (This appears unlikely based on [A]'s letter.) The analysis is similar to that of a suggested minimum donation. (See BTLG Annot. 495.0370 (10/16/72).) If the facts were such that there was no suggested minimum donation, and no obligation to pay [A] even an uncertain amount, we would regard the transfer as a gift even if the church thereafter gave money to [A]. Tax would not apply to that transfer, and [A] would be regarded as the consumer of the tangible personal property she provides as a gift.

We note that an amount charged for installation of the artwork may be excluded from the measure of taxable rentals payable. (Rev. & Tax. Code § 6011(c)(3).) However, it appears that the artwork provided by [A] is fabricated in the process of attaching it to the church. This would be regarded as fabrication labor and not excludable installation labor. We note also that the leases presumably do not begin until after the artwork is created. If this is the case, the artwork must be completed before the can begin. That is a cost of [A] which is passed on to the lessee, and is not excludable from the taxable rentals payable. (See, e.g., BTLG Annot. 330.3310 (7/16/68).) On the other hand, if [A] merely attaches completed artwork to the church, that attachment constitutes installation, the charge for which is excludable from the measure of tax. For example, [A] stated in her letter that her current project is to design and hang 50,000 origami cranes. If the cranes are complete prior to attachment, it is possible that such attachment may be regarded as installation. However, if the attachment is such as to form a unified artwork (e.g., individual cranes attached so as to form a pattern of a crane), that artwork might then be regarded as a unified piece, the attachment of which to the church is regarded as fabrication of the artwork. Unfortunately, this may be a case in which you must apply that well respected legal principle, it's difficult to describe but you will probably know it when you see it.

Supervision

This again depends on the particular facts involved. Apparently, [A] is hired to work with students and others to create a work of art. She is not expected to create the art, but rather to facilitate the artwork's creation by the students. She provides some or all of the materials needed but makes no specific charge for them. The completed art is the property of the church or other person that hires her.

When a person supervises the fabrication of tangible personal property supplied directly or indirectly by the customer, and that supervision is considered to be a necessary component of the fabrication, we consider the supervision to be part of the fabrication of tangible personal property. (Rev. & Tax. Code §§ 6006(b), 6010(b), Reg. 1526.) On the other hand, when a person provides consulting services only, without having control over the performance by others of the fabrication, we regard such consulting services as not part of the fabrication.

[A] provides some or all of the tangible personal property. When she receives any consideration, she is selling that property and some or all of the consideration she receives is subject to tax. If title to the property does not transfer to the purchaser until after the artwork is completed, unless we had further information that convinced us otherwise, we would regard her entire charge as subject to tax. If title transfers prior to the fabrication, a prorated amount of the consideration she receives would be regarded as subject to tax as for a sale of the materials under subdivision (a) of Section 6006. If she controls fabrication of that property into the artwork, the remainder of her consideration would be taxable as for a sale under subdivision (b). If she provides consulting services only, the remainder of the consideration she receives would not be subject to tax.

We hope this information is sufficient to answer you questions in this area. However, we would not be surprised if you had further questions after you receive further information from [A]. If so, feel free to write again.

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David H. Levine